According to London-based securities lending analyst Data Explorers' 2009-10 Securities Lending Yearbook, the second and third quarters of 2009 saw a return of funds flow into Asian equities, closely followed by lenders. Data Explorers says that between January and December 2009, Asian lendable balances rose by 40% from over $500bn to approximately $700bn by the end of the year; though the total was still 30% below the lendable balance in December 2007. The last two quarters of 2009 showed signs of an uptick, not only in terms of volumes, but also in terms of investment by securities lending houses, both in terms of new product and expanding business reach. What will it all mean for business levels in the Asian market in 2010?

A GRADUAL RETURN

Photograph © Rolf Images/Dreamstime.com, supplied February 2010.

GISELLE AWAD, SENIOR vice president, eSecLending, based in Sydney, has witnessed a discernible uptick in confidence and securities lending business volumes in the Asian region through 2009. Awad has noted "a number of beneficial owners re-entered the market in 2009 after having temporarily suspended programs following the Lehman default. In addition, the lifting of short sale bans, improved liquidity, declines in volatility and the rally in world equity markets have contributed the improvement." As for eSecLending itself, the nature of the game was particularly specialised, given that the bulk of the $200bn in assets auctioned globally last year was allocated to agency exclusives, with the balance transacted on a more traditional agency basis.

While the market rejoices in a renewed lending volume as last year closed, the outlook for 2010 is positive, notes Awad, given that eSecLending was appointed lending agent for funds new to lending and also on behalf of funds looking to diversify providers and/or utilize different routes to market.

Scotia Bank notably expanded its securities lending capability through the hiring of a specialist team from Wells Fargo to beef up its Asian operations in September of 2009. Elsewhere, JPMorgan Worldwide Securities Services expanded its securities lending capabilities in the region to take in Taiwan in late November of last year. In the Asia Pacific zone, JPMorgan offers securities lending services in Australia, Hong Kong, Japan, New Zealand, Singapore, South Korea, Taiwan and the Philippines, "some fourteen markets now," notes Andrew Cheng, executive director and head of clients sales management for JPMorgan's securities lending business in Asia ex-Japan , "with the possibility of others coming on stream as well."

Elsewhere, Clearstream opened a new branch in Singapore, run by Robert Tabet, previously head of Clearstream's Dubai office in October last year. According to Philippe Metoudi, head of Clearstream for the Asia-Pacific region, Clearstream's automated securities lending and borrowing services (ASL), and ASL-plus, where Clearstream is the principal borrower and lending and the firm's case by case lending operations, remain cornerstones of its Asia-Pacific business growth strategy. "Over the last five years," acknowledges Metoudi, "overall the Asian region has grown in significance for Clearstream per se, now accounting for almost 20% of its business lines. In the context of securities lending, there are many more conversations around global securities financing, and we find an increasing sophistication among our Asian clients."

Those clients are perforce broker/dealers and central banks. "The pick-up of late has been immense notes Metoudi, with "70% of ASL-plus business located in the Asia-Pacific region." ASL lies at the heart of Clearstream's settlement engine and acts as lender of last resort, explains Metoudi, preventing failures and enhancing the settlement efficiency through automated loans. "With just one contract, borrowers gain access to a large pool of undisclosed lenders, speeding the reception of the proceeds from counterparties. Once the securities are on the account, the loan closes. The ASL Guarantee reduces the counterparty risk for lenders. Lenders can advise Clearstream of the positions available for lending via the lender download facility. This is of particular use to lenders with mixed assets," he says.

Risk management is fundamental to today's business, concedes JP Morgan's Cheng. "Our approach is to give our clients access to risk-adjusted returns. This has always been a focus for us, and it has become a priority for clients." The bank, he says, works closely with clients to reduce as far as possible, the interest rate and credit risk from reinvestment of cash collateral. "What we find in Asia is that Asian asset managers and institutional investors are looking at reducing the risk that they take in a lending programme," highlights Cheng. "Those institutions in co-mingled funds, for instance, which used to take riskier investments, are long gone now. We are telling our clients that our focus is on helping them extract intrinsic value and that risks should be minimised."

That likely involves running segregated cash collateral accounts: "JPMorgan operates with separately managed accounts, which is an unusual model. 100% of our customers in the region utilise them." concedes Cheng. Moreover, he adds, "lenders can adjust the guidelines very easily and we are in a position to react very quickly to changes." Having the ability to control the eligibility of counterparties helps clients mitigate risk more efficiently, he adds, explaining that the bank also provides a robust indemnification programme against borrower defaults, supported by the bank's strong balance sheet". Cheng sees agent lender indemnification (the protection agent lenders provide to beneficial owners against counterparty default) has real value in today's market," he says.

An increased requirement for transparency, the ability to control investment guidelines and a growing awareness of risk mitigation tools are cornerstones of today's securities lending business, states Robert Lees, vice president, head of Securities Lending Trading in Asia for Brown Brothers Harriman (BBH). As regulators become more involved and clients become more demanding, the current requirements are increasingly challenging. Lees highlights that, "The appropriate mix of revenue generation, understanding the underlying client strategy and maximising opportunities in the market against a risk-averse backdrop, has never been more important." He adds that achieving the right mix has been the focus of BBH's program since its inception.'

Changing requirements mean the market must constantly adapt to meet market developments and that encourages further product development. Among the prime movers in this space, in early February EquiLend announced that it intended to expand its services in the

Pertamina Towers, Kuala Lumpur. The Malaysian Securities Commission and Bursa Malaysia spurred SBL based securities lending in the autumn of 2009. Photograph © Szefei/Dreamstime.com, supplied February 2010.

securities lending marketplace by including the ability to borrow and lend ETFs via Trade2O, a service that facilitates the interactive trading of non-GC securities, specials as well as a host of other security types. The initiative "continues to emphasize the flexibility of the platform and highlights its instrument agnostic feature' says Sharon Walker, managing director at Equilend. The move speaks to a variable trend in the region (in fact across the globe) for lending and borrowing ETFs. It is a sign of the times. According to eSecLending's Awad, "there is certainly demand for ETFs in the Asian securities lending landscape, with levels fluctuating on a regular basis."

While Asia remains a growth market, securities lending facilitators are under the cosh to keep up with new product. Some have an immediate advantage: eSeclending, Clearstream and Equilend have clear niches. However, it is not always so easy these days in the global facilitator space. Large houses such as JPMorgan offer their clients a broad array of services, including fund administration, collateral management and depositary receipts, among other services. However, these days not everyone is selling a combined package. Disintermediation is a key trend in Asia, as it is elsewhere. Lees agrees stating that BBH has seen great interest in its third party (non-custodial) lending services. According to eSecLending's Awad, there is a distinct preference for best in class services. "At one time custodian lenders could bank on the fact that their clients regarded securities lending as an ancillary service to custody," she notes. "Now institutions and funds are looking for best in breed providers and will mix and match their mandates accordingly; often separating custody, collateral management and securities lending. It is a different ball game entirely."

It's a view endorsed by JPMorgan's Cheng. "What made sense in 2007 no longer makes sense today. For example, more lenders have brought cash collateral right into the front office; which forces service providers such as ourselves, to

Photograph of Taipei. Taiwan has been more accommodating of securities lending of late. Phtoograph © Rademakerfotografie/Dreamstime.com, supplied February 2010.

become much more focused on liquidity and the maturity of collateral reinvestments. It has ratcheted up the business to a much more sophisticated level and brought us closer to the client in that there is much more discussion these days on the way that collateral is reinvested."

That means constantly pushing the boundaries. In early February EquiLend announced that it will expand its services in the securities lending marketplace by including the ability to borrow and lend ETFs via Trade2O, a service that facilitates the interactive trading of non-GC securities, specials as well as a host of other security types. The initiative "continues to emphasize the flexibility of the platform and highlights its instrument agnostic feature' says Sharon Walker, managing director at Equilend. The move speaks to a variable trend in the region (in fact across the globe) for lending and borrowing ETFs. According to eSecLending's Awad, "ETFs come in and out of focus on a regular basis through the Asian securities lending landscape."

As for JPMorgan's view, Cheng says: "What made sense in 2007 no longer makes sense today. For example, more lenders have brought cash collateral right into the front office; which forces some service providers to become much more focused on liquidity and the maturity of collateral reinvestments. It has ratcheted up the business to a much more sophisticated level and brought us closer to the client in that there is much more discussion these days on the way that collateral is reinvested."

Perhaps because of the willingness of securities services providers to go the extra mile to leverage the business potential of Asia, the upward drive in the market as a whole has buoyed the gradual, yet sustained return of business levels. Equally, there is a growing drive by Asian capital markets to encourage securities lending, or at least allow shorting of stock, in an effort to deepen the region's capital and money markets. Right now, the Asian stock markets have been buffeted by volatility; perhaps not really surprising in this jittery, post recessionary period.

eSecLending's Awad remains buoyant: "The region has transitioned. The dramatic market events of 2008 caused many funds to seek more information about their securities lending programmes. What became apparent is that securities lending is an alpha generating activity and should be treated with the same level of due diligence as any other investment decision. As such, funds should have a comprehensive understanding of the risks and rewards inherent in their programs and feel confident about proper oversight and controls. In addition, there has been an increased amount of independent support for the practice of securities lending from both regulators and academics who view it as an effective mechanism for bringing liquidity and efficiency to the market. It is an important step and the evolution is positive for the industry."

Clearstream's Metoudi is equally upbeat about the region's prospects. By nature the market is volatile in Asia, states Clearstream's Metoudi. Nonetheless, despite temporary market volatility, "I have no doubt the overall trend is upward," he states.

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